

MINUTES
BOARD OF TRUSTEES OF THE
PUBLIC EMPLOYEES' RETIREMENT FUND
143 West Market Street, Suite 500
Indianapolis, IN 46204
June 18, 2004

EXECUTIVE SESSION

Trustees Present

Jonathan Birge, Chair
Richard Doermer, Vice Chair
Garland Ferrell, Trustee
Connie Thurman, Trustee
Robert Welch, Trustee

Others Present

Craig Hartzler, PERF Executive Director
Bruce Kimery, PERF Deputy Executive Director/Chief Benefits Officer
Leisa Julian, PERF General Counsel

The Board met in Executive Session to discuss matters under IC 5-14-1.5-6.1(b)(7) and IC 5-14-1.5-6.1(b)(5).

REGULAR SESSION

Trustees Present

Jonathan Birge, Chair
Richard Doermer, Vice Chair
Garland Ferrell, Trustee
Connie Thurman, Trustee
Robert Welch, Trustee

Others Present

Tony Aaron, Ice Miller
Elaine Beaty, McCready & Keene
Mary Beth Braitman, Ice Miller
Douglas Todd, McCready & Keene

PERF Staff Present

Craig Hartzler, PERF Executive Director
Bruce Kimery, PERF Deputy Executive Director/Chief Benefits Officer
Leisa Julian, PERF General Counsel
Will Frayer, PERF Staff Attorney

Michael Horstman, PERF Chief Financial Officer
Patrick Henn, PERF Staff Internal Auditor
Patrick Lane, PERF Director of Outreach Services
Cindy Osborne, PERF Minute Writer

ITEMS MAILED TO THE BOARD PRIOR TO MEETING

- A. Board Update
- B. Board Book

I. APPROVAL OF MINUTES

MOTION duly made and carried to approve the Minutes of the May 12, 2004 Board of Trustees Meeting.

Proposed by: Garland Ferrell
Seconded by: Connie Thurman
Votes: Five in favor, 0 against, 0 abstentions.

MOTION duly made and carried to approve the Minutes of the May 21, 2004 Board of Trustees Meeting.

Proposed by: Garland Ferrell
Seconded by: Connie Thurman
Votes: Five in favor, 0 against, 0 abstentions

II. OLD BUSINESS

- A. Building Update. Mr. Lane provided a brief update on the status of the 143 W. Market Street building renovation project.
 - Mr. Lane indicated that we are currently on schedule and are still on budget.
 - PERF switched to a new plumbing system a week ago.
 - Mr. Lane reminded the Board that all restrooms on floors five through eight are closed during this phase of the construction process.
 - The renovation project should be completed by July 30, 2004.
 - Mr. Hartzer added that our building now has new signage.
 - The Board was issued security passes to enter the building, but Mr. Lane explained that once we switch over to our new security system, the Board will get new passes.

- Mr. Lane informed the Board that PERF will also have an overhead canopy at the front entrance (the Capitol Street side). The canopy will be suspended by a cable and should match the profile of our current canopy on the Market Street side of the building.
 - Flag poles will also be installed at the front entrance.
 - Mr. Hartzler told the Board that Mr. Lane has done a great job with this project. The renovation of this building will be much better for our members and their families, our staff, and for the Board of Trustees.
 - Mr. Birge expressed his appreciation for a job well done.
- B. Sale of 125 W. Market Street Building. Mr. Hartzler reminded the Board that PERF has accepted an offer on the 125 W. Market Street building. He indicated the closing has not taken place yet. Ms. Julian added that the closing is planned to take place by August 31, 2004.
- C. Employer Education/Outreach. Mr. Hartzler noted that PERF will be adding two additional staff to the outreach services area. Mr. Hartzler explained that PERF needs to have a strong partnership with the employers. PERF will have an aggressive schedule of getting to even more employers with the help of the new staff.
- Mr. Lane agreed that having a partnership with our employers is key.
 - The outreach program was created a couple of years ago. PERF has taken an incremental approach to determine what could be accomplished with a small investment. We are looking to expand upon that investment.
 - The outreach mission is to improve the education of our members and the training of our employers.
 - Within the last few weeks, PERF has had a couple of employer training sessions that rolled out the “big three processes,” which are retirement applications, wage & contribution reporting, and new member enrollments. These initiatives are changing the way PERF interacts with employers on a day-to-day basis.
 - Mr. Lane noted that there is a lot of turnover at the employer level and reeducation is very necessary. This is an ongoing challenge for PERF.
 - We’ve already seen very positive comments regarding our new outreach efforts. As we roll out this fully resourced outreach program, we’ll be able to look at statistical data that we have created thus far.
 - Mr. Hartzler said that the outreach area has done a great job with the limited number of staff that they currently have, and the

assistance of the additional staff will give us a tremendous boost for employer relations.

D. Quality Assurance/Risk Management. Mr. Hartzler explained to the Board that with PERF's 2005 budget, we will be creating a new quality assurance/risk management unit. This unit will have a staff of four.

- Mr. Hartzler reminded the Board that he has been talking with Mr. Claud Davis from Irwin Financial. Irwin Financial is recognized as one of the "best in class" for internal controls and audit functions. Mr. Davis has offered to come to a Board meeting to share with the Board best practices and lessons learned at Irwin. PERF has asked Mr. Davis for references about other pension funds that he is familiar with and we are asking for assistance with job descriptions for the new unit.
- Mr. Hartzler noted that Irwin periodically hires a CPA firm to come back in and validate some of their corrective action plans in the middle of a calendar or fiscal year to ensure that the improvements are being made.
- Mr. Hartzler explained that PERF is considering many of these options as we go forward in this area.
- Mr. Kimery added that years ago the emphasis on risk management and internal audit was more on the investment side. PERF will now have the staff to look at both the investment aspect of the agency as well as the operations side of things.

E. Indiana Pension Systems Inc. (IPSI) Business Services Agreement. A copy of the Information Services Agreement and a one page summary of that document were handed out to the Board. Ms. Julian explained that IPSI is still in its formative stages. The formal documents are still being prepared. Mr. Aaron, attorney with Ice Miller, provided the following summary of the Agreement.

- Mr. Aaron explained that this is a three-party agreement between PERF, TRF and IPSI.
- The scope of the services that IPSI will providing under this Agreement are those services that Covansys is currently providing – primarily those related to the SIRIS system.
- The Agreement is designed so that additional information technology and related services could easily be added by adding the services to a schedule. Similarly, if there was a desire to remove services from the Agreement, this could be done, as well.

- The Agreement is for an initial term of five years. It is designed so that it is a rolling five years. The Agreement is effective on July 1, 2004. Next July 1, there would be an additional year added to the term. That rolling five-year term can be terminated on 90-days' notice. In addition, there's an option to terminate the Agreement anytime after the first year, upon six months' notice.
- The rate structure provides that most actual expenses of IPSI will be split 50/50 with the exception of the developers and the developer team leads who are assigned to each of the Funds. Each Fund will be billed at an hourly rate based upon that developer's salary or their hourly rate for hours worked for each particular fund.
- PERF and TRF have the right to approve certain positions.
- The Funds retain ownership of any modifications to SIRIS.
- IPSI is required to maintain standards to safeguard data and information that are no less rigorous than those of each of the Funds.
- Ms. Julian explained that the IPSI Board reviewed the document thoroughly. The Board approved the document yesterday and it is scheduled to go to the TRF Board on July 1, 2004.
- Ms. Julian noted that it is being presented to the Board today to allow IPSI to stay within their "completion of the documents" timeline to formalize IPSI entirely.
- Mr. Ferrell noted that the Board members have not had the opportunity to review the document.
- Ms. Julian commented that she understood Mr. Ferrell's concern and apologized that it was not available sooner than it was. It took a lot of time for the IPSI Board to review the document and make all the necessary changes. However, it has been approved. Ms. Julian reminded the Board that there are representatives for both PERF and TRF on the IPSI Board.
- Mr. Birge explained that because we have two knowledgeable PERF representatives on the Board, he feels comfortable with the document at their recommendation. He is reluctant to slow down this process.

MOTION duly made and carried to approve the Indiana Pension Systems, Inc., Services Agreement as presented.

Proposed by: Richard Doermer
Seconded by: Connie Thurman
Votes: Five in favor, 0 against, 0 abstentions

- F. 1977 Police and Firefighter Pension Fund Employer Contribution Rate. Mr. Hartzler reminded the Board that the rates for all of the Funds except the 1977 Police and Firefighter Pension Fund have

been set. This rate was not set because Mr. Todd was doing an experience study of the 1977 Police and Firefighter Pension Fund, and it was not completed at the time the other rates were set. The experience study was the recommendation of the Milliman Actuarial Audit. Mr. Todd provided the following overview of the actuarial experience study.

- An experience study is where the actual experience of the pension plan is reviewed and compared to the assumptions that are made and then liabilities are determined.
- Mr. Todd noted that he made proposed changes when he did this study. He utilized his proposed changes when he did the July 1, 2003, valuation.
- When he did the July 1, 2003, valuation with the revised assumptions, he came up with a contribution rate of 20.2% of first class salaries. Despite this result, he is continuing to recommend the 21% rate.
- The study demonstrates that the actual assumptions currently being used had a margin of conservatism.
- The only plan that didn't use a 7.25% interest rate assumptions was the 1977 Police and Firefighter Pension Fund. Mr. Todd noted that they are now lining it up so that the interest rate assumptions is the same throughout all the Funds.
- There wasn't enough experience with the mortality rate. Mr. Todd is recommending the Fund use the same mortality assumptions that PERF is using.
- The current future salary increase assumption is presently at 5.0%. In reviewing the rate for the past several years, Mr. Todd noted that it has always fallen below 4.0%. The recommendation is that the salary increase assumptions be lowered from 5.0% to 4.0%.
- Mr. Todd explained that the cost-of-living adjustment is different from other Funds where the cost-of-living is ad hoc. The 1977 Police and Firefighter Plan has statutory cost-of-living adjustment. It's based on the cost-of-living adjustment, but can't exceed 3.0%. A 3.0% assumption has been in effect since 1978 and has been fine. Lately the rate has dropped below 3.0%. They are now recommending a change to 2.75%.
- The recommendation for the retirement rates for retirements between ages 50 and 70 was bumped up to 50.0%.
- The post-disablement mortality rate assumptions recommendation is 115.0% of UP-94.
- Mr. Todd recommended no change in the disability and turnover assumptions rates.

Mr. Todd provided a handout to the Board that summarized the cost results based on the January 1, 2003, actuarial valuation. The employer contribution as a percent of salary prior assumptions was 27.8%. The proposed assumptions with 30-year amortization is 20.2%. The proposed assumptions with 13.6-year amortization is 21.0%. The proposed assumptions with a 10-year amortization is 21.6%. The funded status prior assumptions was 82.0%. The proposed assumptions with a 30-year amortization is 94.0%; with a 13.6-year amortization is 94.0%; and a 10-year amortization is 94.0%

Mr. Todd also provided a handout that showed the funded status of each of the defined benefit plans administered by PERF.

MOTION duly made and carried to adopt the actuarial rates as presented.

*Proposed by: Garland Ferrell
Seconded by: Robert Welch
Votes: Five in favor, 0 against, 0 abstentions*

G. Committee Reports.

1. Investment Committee. Mr. Doermer noted that all trustees were present during the Investment Committee meeting. The Committee discussed the following.

- A \$30 million commitment for investment in Merit Mezzanine Partners, which is a debt-related private equity segment of the total alternative investments.

MOTION duly made and carried to approve the \$30 million commitment for investment in Merit Mezzanine Partners.

*Proposed by: Garland Ferrell
Seconded by: Robert Welch
Votes: Five in favor, 0 against, 0 abstentions*

- A change in the mix of the alternative investments was recommended for Board approval. The purpose is to enhance the flow of income to the Fund and to have smaller exposure to risk. It was also decided to shelve a considered investment in hedge funds. In regards to buyouts, there was a

42.5% target out of the overall 5% investment figure and we would reduce that from 42.5% to 30.0%. All changes were identified in column "B" of the exhibit under Tab 4 in the Board book.

MOTION duly made and carried to approve the recommended changes in column "B" under Tab 4 of the Board book.

Proposed by: Richard Doermer
Seconded by: Garland Ferrell
Votes: Five in favor, 0 against, 0 abstentions

- An update was provided by Mr. Duncan at the Investment Committee meeting on the search for a large cap value manager. Royce Low Priced Stock Fund was recommended for Board approval for the \$2.2 million Legislators' Defined Contribution Plan.

MOTION duly made and carried to approve the selection of Royce Low Priced Stock Fund as the new large cap value manager.

Proposed by: Richard Doermer
Seconded by: Garland Ferrell
Votes: Five in favor, 0 against, 0 abstentions

- The Committee voted for Board approval the rebalancing recommendation within the domestic equity sub-asset class as presented by Mercer in a handout dated June 15, 2004.

MOTION duly made to approve the rebalancing recommendation as presented in the Mercer handout dated June 15, 2004

Proposed by: Connie Thurman
Seconded by: Richard Doermer
Votes: Five in favor, 0 against, 0 abstentions

2. Benefits Administration Committee. Ms. Thurman noted that all trustees were present during the Benefits Administration Committee meeting. The following is the highlights from that meeting.

- PERF processed 200 retirements and 903 ASA refunds.
- We received a good response from the Customer Service Questionnaire.
- The three major system changes – electronic reporting, retirement process, and new employer records were discussed.
- The Committee voted for Board approval, the line-of-duty death claim for Scott A. Patrick and the line-of-duty death claim for James E. Baugh in the amount of \$150,000 each.

MOTION duly made and carried to approve the line-of-duty death claim for Scott A. Patrick in the amount of \$150,000.

Proposed by: Connie Thurman
Seconded by: Richard Doerner
Votes: Five in favor, 0 against, 0 abstentions

MOTION duly made and carried to approve the line-of-duty death claim for James E. Baugh in the amount of \$150,000.

Proposed by: Connie Thurman
Seconded by: Robert Welch
Votes: Five in favor, 0 against, 0 abstentions

3. Audit and Budget Committee. Mr. Ferrell noted that all trustees were present during the Audit and Budget Committee meeting. The following are the highlights from that meeting.

- There was a discussion on internal tax reporting. Most findings have been corrected.
- An update on the audit plan was provided.
- An update on the outstanding audit comment was provided.

- III. REPORT OF EXECUTIVE DIRECTOR. Mr. Hartzler reminded the Board that we have not yet selected a firm for the RFP for internal controls, prior retirement payments, and refund balances and payments. A decision will be made soon.

We continue to make progress on our “Yellow Brick Road.” All eleven goals have been updated. Mr. Hartzler noted that although we can

never forget where we've been, neither can we forget where we're going.

Mr. Kimery added a brief update on the financials. He indicated that PERF will end the year on a positive note. Copies of the financial are available for review under Tab 15 in the Board Book.

IV. ADJOURNMENT

There being no further business, the meeting was adjourned.